No. 20480

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JOHN N. NEWLAND, Trustee in Bankruptcy for HUGHES HOMES, INC., a Montana Corporation, and HUGHEST HOMES ACCEPTANCE CORPORATION, an Idaho corporation

Appellant,

vs.

WINCEL T. EDGAR and HELEN E. EDGAR, husband and wife,

Appellees.

BRIEF OF APPELLEE

Appeal from the United States District Court
for the District of Idaho,
Northern Division

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Sandpoint, Idaho

TEXTS AND STATUTES

INDEX

AUTHORITIES

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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r HUGHES HOMES, INC., a Montana
rporation and HUGHES HOMES ACCEPTANCE
RPORATION, an Idaho Corporation ,

Appellant,

vs.

NCEL T. EDGAR and HELEN E. EDGAR,
sband and wife,

Appellees,

BRIEF FOR APPELLEE

In this diversity action, the appellant rporations have urged that the United States strict Judge did not correctly apply the e Lanzarotti rule, United States Building d Loan Association v. Lanzarotti, 1929, Idaho 287, 274 P. 630-632, which Lanzarotti le was thoroughly analyzed and discussed by e United States Circuit Court of Appeals, nth Circuit in the Whitman case, Whitman v. eene, 1961, 289 P.2d 566.

STATEMENT OF THE FACTS

ppellees, residents of Idaho, and the rtgagors herein, brought action for cancelli-on of an allegedly usurious note and mortgage, for judgment for penalty under the Idaho ry statute. Appellees named as party defend- to their action Hughes Homes, Inc., a tana corporation, to which the note and rtgage were made payable. This corporation, ch will be referred to herein as the Mont- corporation, appeared generally in the ion, being represented by John N. Newland, stee, appointed by the United States District rt in Montana bankruptcy proceedings.

ughes Homes Acceptance Corporation, an Idaho poration, also represented by the same Newland as its Trustee in bankruptcy pro-dings, appeared generally in the action,

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ıd sought leave of the court to be joined as party defendant. By stipulation, Transcript ıge 26, Order was entered bringing this Idaho ırporation in as a party defendant. Being the ıly Idaho corporation herein involved, it .ll be referred to herein as the Idaho corıration.

The Idaho acceptance corporation alleged the ısignment to it of the note and mortgage ıvolved, and sought foreclosure of the same. The note and mortgage called for interest the rate of 10% per annum, usurious as ;ainst the legal maximum in Idaho of 8% The Montana corporation defended against ıpellees' claim on two grounds: that the

[illegible]

[illegible]

[illegible]

tire transaction out of which the obli-
tion secured by said note and mortgage
ose, took place in the state of Wash-
gton, and is controlled by Washington
w, and; that in fact only 8% interest
s collected and charged the appellees.
. p. 30.

The Idaho corporation, in its Answer and
oss-complaint, alleged: that all of the
tes, debts and obligations evidenced
said note and secured by said mortgage were
ntracted for, consummated and executed in
e state of Washington.

Appellants, at the trial, Rep. Tr. p. 20,
d in their brief, have invited attention
Anaconda Building Materials v. John N.
wland, 1964, 336 Fed 2d 625, which
volved the same parent Montana corpora-
on, the same Idaho acceptance corporation,
d three other subsidiary corporations, one
Washington, one of Wyoming, and one of

ntana. In that case it was held by the rcuit Court of Appeals that all of the ve corporations of the Hughes enterprise re separate entities, and noted that each bsidiary was totally owned by the parent ntana corporation. It was also noted that . C. Hughes, Jr., was president of each rporation, dominating and mismanaging e entire enterprise

The note and mortgage involved encumbered aho real property owned by the appellees, d both are exhibits to appellants' plead-gs, and in evidence. Also placed in evidence the assignment by which the Idaho corporation quired the mortgage. Defendant's Exhibit . 3.

The assignment was never recorded. No assign-nt of the note seems to appear, but the signment of the mortgage states "together th the obligation thereby secured and the

omissory Note evidencing the same,"
d, it was stipulated formally that
e note was assigned to the Idaho
rporation on October 10, 1960, also
e same date as the unrecorded assignment
the mortgage.

The note and mortgage called for 120
nthly payments. The Idaho acceptance
rporation, by the assignment, came into
nership of the same with 119 of these
nthly payments, computed at 10% per annum
terest, yet to be made. The appellees made
o payments to the Montana corporation, one
which was made after the assignment, and,
en, until the appointment of Mr. Newland,
de ten more payments to the Idaho corpora-
on, all of which payments were sent by the
pellees to Montana, and were then sent on
Blackfoot (Idaho) for deposit. Rep. Tr.
21, 1. 7.

[illegible]

[illegible]

[illegible]

The note was made payable at Butte,
ntana, and on a ten-year basis of 120
nthly payments, to retire $5,445.30,
gether with the stated interest of 10%,
quired payments of $71.37 per month.
y bank amortization schedule will confirm
at $71.37 per month is required to retire
,400.00 in ten years at ten per cent.
It was formally stipulated to by the
rporations that as payments were received,
o monthly receipt was sent to the plaintiffs
ppellees) showing the application of payments
ceived to principal and interest." And, at
e trial Mr. Edgar, appellee, testified that
ere was never a time after he and Mrs. Edgar
gan making payments that they were given any
vice from either corporation as to what rate
terest was being computed at, or but what
ey would be making the 120 payments required
them. Rep. tr. p. 8, lines 8-21.

It was formally stipulated to that the
ntana corporation's agent for this trans-
tion here involved was also a realtor
censed to do business in both Idaho and
shington, with a residence and only office
Newport, Washington. And also formally
ipulated that the appellees were Idaho
sidents, and the nearest city to their
sidence was the town of Newport, Washington.

It was testified to by Mr. Edgar, <u>without
ntradiction</u>, that the "dealing" primarily
ok place at appellee's home in Idaho, and
e signing of the papers was in Newport, and
at Mr. Jones, the notary to the mortgage,
d no part in the transaction other than to
t as notary. Rep. tr. p. 7, l. 19-25;
18, l. 4-7

The U. S. District Judge found <u>against</u> the
ntention of appellants that "the entire
ansaction took place in the state of

shington and is controlled by Washington w," and applied the rule of <u>Lanzarotti</u>.

The district court found from the evidence lduced in court and from the evidence set rth in the stipulation of the parties, that e signing of the note and mortgage at Newport, shington, was a mere matter of convenience.

On the issue of knowledge and lack of good ith on the part of the corporations the court ted that the corporations took the precaution entering computations on its own books at aho's legal rate of 8%, but for a period of most four years failed to advise the appellees at they were being charged anything less than e 10% interest exacted of them on the note d mortgage.

The first written contract for the sale of e prefabricated house, Defendant's Exhibit . 4, was signed on July 6, 1960, some 12

ys before the appellees signed the note and rtgage.

During this 12 day period of time, the contract, fendants' Exhibit No. 4, calling for 120 monly payments of $68.01 which is just under 9% r annum, ripened into the note and mortgage lling for the payments of $71.37, at 10% r annum. ($5400.00 at 8½% on ten years requires yments of $66.96; $5400.00 at 9% on ten years quires payment of $68.41)

The contract, Defendants' Exhibit No. 4, is a printed form of the Montana corporation. e note and mortgage are also on its printed rms, the mortgage specifically providing:

"This mortgage is executed with the mutual understanding that the prefabricated house or building purchased from Hughes Homes, Inc., under the contracted dated July 6, 1960, shall be erected * * * *."

Defendants' Exhibit No. 2

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[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

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The U. S. District Judge in applying the w to the facts of the case, stated that the st recent case involving the Lanzarotti rule me from the Ninth Circuit Court of Appeals, itman v. Greene, 1961, 289 Fed 2d 566, and e gist of the appeal is appellants' con- ntion that the Lanzarotti rule was incor- ctly applied, and that the District Judge's ndings are improper and unsubstantiated.

In the Whitman case, the Circuit Court con- uded by stating, as applied to that case:

"Under these circumstances we feel that the Lanzarotti rule must be read to apply to those cases involving the doing of bus- iness within the state of Idaho, and a purpose to evade the usury laws of that state. In the case at bar the lender did not seek out the borrower in the state of Idaho, nor sit in wait for him in that state. Rather, the borrower sought out the lender in the State of Washington."

The Lanzarotti rule was spelled out in the inion, quoting directly from United States

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ilding and Loan Association v. Lanzarotti,

29, 47 Idaho 287, 274 P. 630-632:

> This court stands committed to the rule that ''this being purely an action in rem, and the enforcement of the claim being only maintainable in Idaho,' it cannot be contended that the intention of the parties was that the laws of 'Montana' should obtain in the construction of the contract.' (citing Vermont Loan and and Shea)"

The Circuit Court analyzed Zimmerman v. own, 1917, 30 Idaho 640, 166 P. 924, in aching the conclusion of the Whitman case, d noted from Zimmerman the lack of "proof bad faith or of an effort to evade the ury laws of this state," noting therefrom at it was not the in rem aspect which was e true basis of the Lanzarotti rule.

The United States District Judge in the se at bar applied the rule as so defined, nding that the Montana corporation, quali- ed to do, and doing business in Idaho, ok a note and mortgage usurious by Idaho

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[illegible]

atute, and that payments were taken and ceived by both corporations.

As to the proof of bad faith, or of usurious tent, requisite proof of which as an sential was suggested in Whitman, the strict Judge found a purpose to evade the ury law of Idaho, and noted the failure of e appellant corporations to advise appellees at they were being charged any less than the % per annum stipulated for in the note.

Appellants' Concessions

Appellants seem to concede that the Montana rporation is chargeable with the preparation the note and mortgage, Appellants' Brief, 30 -- which concession is justified by the ct that the same were drawn on printed forms tting forth the corporate name, and appellee . Edgar testified that the notary only acted a notarial capacity.

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[illegible]

the top of page 32, Appellant's Brief, is ated the concession that the Montana rporation is charged with knowledge that e maximum legal rate of interest in Idaho s 8%.

On the top of page 37, Appellant's Brief, is ted the distinction between the position of e Idaho acceptance corporation, here an signee of the non-negotiable mortgage, to- ther with the debt thereby secured, and an dorsee in due course of negotiable paper thout actual notice of usury.

In the next to last paragraph of page 37, pellants' Brief is correctly stated that the aho usury statute "also makes provision for penalty to be suffered by the person to whom urious interest has been paid."

Finally, on page 38 of Appellants' brief is ated:

"As appellant has urged, the Lanzarotti case is one wherein it was virtually held as a matter of law that a foreign corporation cannot loan money in Idaho, and reserve and collect interest in excess of the statutory maximum."

Contentions of Appellants

Examination of the facts and circumstances the case, and a reading of the brief of pellants, including the foregoing conssions of the appellants, seems to indite the gist of appellants position on peal to be that stated on the bottom of ge 38, Appellants' Brief, whereat the pellants say that the District Judge's termination that there was both a doing business in Idaho and a purpose to evade aho law were erroneous conclusions of law, l not findings of fact at all.

Argument

Appellants cite to the Court the case of ndgren v. Freeman, 1962, Ninth Circuit, 307 d 104. In this case the Circuit Court resolved e question of whether or not the "clearly er-neous" provisions of Rule 52 (a) F.R. Civ. has application where it is contended on peal that the credibility of the witnesses not involved. The holding of the court was:

> "Rule 52 (a) explicitly clearly applies where the trial court has not had an opportunity to judge of the credibility of witnesses."
>
> Lundgren v. Freeman, supra
> At 114 of 307 F2d

It is submitted that the appellants go far ield in citing this case, for the reason at witnesses did testify in the case at r, and it was for the District Judge to termine the credibility to be attached to e testimony of Mr. Edgar which established

at the transaction leading into the note d mortgage was an Idaho transaction.

In any event, the "clearly erroneous" le here applies, and it was the province the trier of the facts to determine ere the transaction took place, and to nd as a fact the evasion of Idaho law, d of bath faith on the part of the app- lants.

"Rule 52(a) should be construed to encourage appeals that are based on a conviction that the trial court's decision has been unjust; it should not be construed to encourage appeals that are based on the hope that the appellate court will second-guess the trial court."

Lundgren v. Freeman, supra at 114 of 307 Fed 2d.

This Edgar case, to be now decided by the rcuit Court is, as stated by the District dge, "practically on four squares with e quoted factual situation in Lanzarotti." . p. 53. Moreover, it is, from the

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tandpoint of an attorney or jurist

aving had "experience with the main-

prings of human conduct" (Lundgren),

case more deserving of judicial con-

emnation and in stronger language than

as used in Vermont Loan and Trust Co.

Hoffman, 1897, 5 Idaho 376, 49 P. 314,

5 Am. St. Rep. 186, 37 L.R.A. 509, where

ie Idaho Supreme Court said, and the

inth Circuit Court of Appeals quoted

ierefrom:

"The proposition simply states this: A foreign corporation, having a resident agent in this state, engaged in the business of loaning money upon interest, may avoid the laws of this state in regard to such business, and especially in regard to usury, by simply making the evidences of indebtedness payable in some other state, where the laws against usury are less onerous. The monstrosity of the proposition is tooapparent to require comment. * * *"

Vermont Loan v. Hoffman,
supra
Whitman v. Green, Supra
(emphasis added)

[illegible]

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[illegible]

We have here an Idaho corporation owing its
ry existence to the laws of the state of Idaho,
d which was formed specifically for the pur-
se of buying from the parent Montana cor-
ration which borned it, mortgages on Idaho
al property. We have this Idaho corporation
ying and owning a mortgage on the real pro-
rty of Idaho citizens, with the interest on
e face set at 10%, and receiving and accept-
g monthly payments computed at that usurious
te of interest. We have, to borrow language
om the Vermont case, the monstrosity of an
aho corporation acquiring, from its parent
ntana corporation, a ten-year, 120-payment
te, with 119 payments yet to be made, the
ansaction supposedly purified by the mortgage,
d note secured thereby, momentarily passing
rough the hands of the foreign parent
rporation.

But, then we have, too, the foreign
irent corporation also a corporation author-
:ed to do and doing business in Idaho in com-
:tition with other building corporations,
ıking the mortgage and note, encumbering
laho realty, at a rate of interest prohibited
› its Idaho competitors, and doing so with
forehand knowledge that the same would be
mediately sold and assigned at a discount to
s domestic, Idaho subsidiary corporation, in
mpetition with other Idaho finance corporations.
Called before the bars of justice, we have
th of these corporations, the Montana
rent, and the Idaho subsidiary, pleading
nocence, and on the boot-straps of their own
fice records alone, claiming that the penalty
ould not be applied where their own cor-
rate records showed the transaction was being
corded the same status of its fifty some other
aho transactions, and interest being computed

8% rather than the 10% stipulated for the note and mortgage.

Yet, caught on the horns of a dilemna, while urging that usury was not exacted on the rporate records because it was treated as Idaho transaction, the appellants contin- to argue before the Circuit Court of Appeals at this was not an Idaho transaction at all. And, at the same time, because it is the uth, the appellants have admitted that from e time of signing the note and mortgage on eir Idaho realty, there was never a time at the appellees were ever advised of the od news that they were in actuality being arged only 8% interest.

Any court of law or equity would require of e appellants that they informed the appellees cordingly. But they did not, not the Mont- a corporation, not the Idaho corporation,

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ad not the trustee appointed for each.

In turn, all accepted payments based on

the charge of 10%.

While it is true that the 10% rate was

charged and reserved by the Montana corpora-

tion, it was not only paid to that corporation.

but to the Idaho corporation as well. An old

Idaho case seems to be in point, and contains

appropriate comment:

"It is well settled, that a usurious contract may be purged of every taint of usury. (Webb on Usury, Sec. 482 et seq.) In section 482 that author says: 'Of course, if no usury has been paid, but merely reserved, it is sufficiently purged by a surrender of the contract, and the giving of a new one with the element of usury excluded.' It is also held that, if usury has been paid, the refunding of it, and its acceptance by the person in interest as such, under the agreement that only legal interest shall thereafter be charged, frees the contract from the taint of usury. It is well settled that parties can cancel and destroy the one contract, purge the consideration of usury, and make it the basis of a new obligation , and thereby bind the borrower, in law and equity, to pay the money actually received on

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"and a legal rate of interest therefor. (Webb on Usury, Sec. 291, and authorities there cited.) That was done in this case. The intention of the appellant and respondents in making the renewal contract was to purge the old contract of usury, and destroy it and to make the new contract free and clear of all taint of usury; and they accomplished their intention. The offense of usury conissts in taking unlawful interest, and in many states the penalty is quite severe, going to the forfeiture of the entire principal debt."

Sanford v. Kunz
9 Idaho 29, at page 34
71 Pac 612

As a matter of law, the, the appellants, ıd each of them, had the opportunity of pur-ıng the note and mortgage of usury by offer-ıg a new contract. This was not done, and ıe District Judge properly held:

"The defendant knew the interest to be improper, as evidenced by the fact that on the defendant's books the interest on each payment was charged at 8% (legal in Idaho). This certainly shows a knowledge by the defendant of a legal rate of interest in Idaho. Yet for a period of almost four years, the defendant and its

"assignee failed to advise the plaintiff that any lesser interest was being charged."

Tr. p. 54

ere clearly was the proof of effort to evade he usury laws of this state, and also proof of ad faith, both mentioned in the Zimmerman case, nd quoted in Whitman.

Here was a case where appellants both in the rial court and now before the appellate court rge that the transaction was one of the state f Washington, and yet the mortgage was not ssigned to the Washington subsidiary, but to he Idaho subsidiary.

Paraphrasing from the Lundgren case, page 115, nd the first paragraph of the second column, he trial judge's findings of intent to evade daho law and of bad faith, and that the transaction was an Idaho transaction governed by the ule of Lanzarotti were not derived from application of legal standards, but from the trial idge's experience with human affairs.

"Therefore, we may not substitute our judgment if conflicting inferences may be drawn from the established facts by reasonable men, and the inferences drawn by the trial court are those which could have been drawn by reasonable men."

Lundgren v. Freeman, supra at page 113, first column

: is submitted that the trial court, and now ie appellate court, are being asked too much iere appellants continually argue that appellees ere charged only 8%, on the basis of Defendants' hibit No. 6. So long as the appellees were ying on a note that called for 120 payments $71.37 each, predicated upon a charge of 10% terest, and payments at that rate were paid appellants, and received without any advice the contrary being given appellees, the strict Judge was correct in finding that both pellant corporations were paid and knowingly ceived interest at a rate usurious by Idaho w.

page 22 of appellants' brief, appellants
rge that Lanzarotti can not be applied unless,
appellants say the fact of the matter was
Lanzarotti, all of the elements of the
ansaction are referable to one situs.

To which it may be replied that in Lanzarotti
l of the incidences of the transaction were
t referable to one situs. In particular, the
te was payable in Montana, the incident or
ement of place of performance, and presum-
ly in Cornelison v. United States Bldg. &
an Association, 1930, 50 Idaho 1, 150 P.
55, the note was likewise payable in Mont-
a. There is no justification for appellants
argue at page 23, appellants' brief, that
e case at bar is dissimilar from Lanzarotti,
rmont Loan, and Cornelison because of
oreign subject matter and foreign contact."

On evidence virtually without conflict or
ntradiction, the District Judge found that

ie Montana corporation was doing busi-
ess in Idaho, and that it sought out the
ppellees in Idaho, sold them a prefabri-
ited house in Idaho, and financed the same
' a note and mortgage of Idaho realty, the
ote being usurious on its face, with the
rtgage to be immediately assigned to an
aho subsidiary corporation. The "foreign
ntract" here is no different than it was
Lanzarotti -- the making of the obliga-
on payable in Montana.

One other minor point should be mentioned.
e mortgage purchased by the Idaho subsidiary,
d assigned to it was not "negotiable paper"
ference to which is made in sec. 27-1907 I.C.
e mortgage was not endorsed to the Idaho
rporation, but assigned, and, moreover, this
s correct, because it could not be negotiable
th the following provision therein contained:

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[illegible]

[illegible]

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[illegible]

[illegible]

[illegible] possible in [illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

"This mortgage is executed with the mutual understanding that the prefabricated house or building purchased from Hughes Homes, Inc., under the contract dated July 6, 1960, shall be erected * * * etc * *."

Mortgage, Defendants' Exhibit No. 2

'An instrument which contains an order or promise to do any act in addition to the payment of money is not negotiable. * * *"

Sec. 27-105 I.C. Uniform Negotia
Instruments Law

it is settled law that a bill or note, whether gotiable or non-negotiable, may be transferred om one person to another in various ways. It y be transferred by negotiation, either by livery or by endorsement. Or, as was done here, per whether negotiable or non-negotiable, "may transferred by assignment. The Uniform Act es not prevent the transfer of a negotiable strument by assignment. In fact it recog- zes that a transferee is not always a holder due course. It is clear, however, that an signee takes generally only such title as his signor subject to all defenses available

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ainst his assignor." 8 Am Jur. 38-40, Bills
Notes.

The Idaho usury statute itself, 27-1907, C., does not excuse even an indorsee of gotiable paper, unless he does not have tual notice of the usury.

In the case here under consideration, the pellants have commendably at the bottom of ge 37, appellants' brief, acknowledged to e court that the Idaho statute, in the cond sentence, specifically makes liable e person "taking or receiving" usurious terest, and it was exactly this provision the statute under which the District dge held the Idaho acceptance corporation able:

> "In case the greater rate of interest has been paid, the person by whom it has been paid, or his legal representative, may recover back the amount of

[illegible]

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[illegible]

[illegible]

"interest thus paid from the person taking or receiving the same, plus twice the amount of such interest in addition."

27-1907 I.C.

is was not only a non-negotiable mortgage, e mortgage carrying with it the note, and t the reverse, but it was assigned, and e 10% rate, amounting to usury under Idaho w, showed on the face. The assignee not ly is thus charged with knowledge of what e assignor did, but the assignee itself ok and received all of the payments other an the first one.

The note in question calling for 10% interest s usurious on its face. And the following atement of the Idaho Supreme Court in the <u>rnelison case</u> is appropriate here:

"* * the contract sought to be enforced is shown upon its face to be usurious.* *"

"Though the lender may not intend to be guilty of usury, yet he is nevertheless guilty for he intends to do what he does but mistakes the law."

[illegible]

[illegible]

[illegible]

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[illegible]

"The contract was drafted by appellant or its agent, presented to and signed by respondents, and payments received thereunder. It would therefore hardly be consistent to hold upon the record before us that there was no violation of the provision of C.S. sec. 2554, in that appellant did not knowingly receive, reserve or charge a rate of interest greater than that allowed under the provisions of said section."

"There is ample evidence to support the court's finding 'that the defendants knowingly charged a rate of interest in excess of 10% per annum and that the contract is a usurious contract under the statutes of the state of Idaho."

Cornelison v. U.S. Bldg. Assn. 1930, 50 Idaho 1, 292 Pac. 243

The Idaho corporation was owned by the Montana corporation. Both were doing business in aho, one in the state of its creation, and e other by properly qualifying. Each had the ne president. The Anaconda case clearly shows at the Montana corporation made its sales Idaho, including this one to the appellees, immediate assignment of the mortgage to

ıe Idaho corporation. All of this was ıown to both of the corporation. And, then, ı top of such circumstances, both participated ı collecting payments based on 10% interest, ıd made book-keeping entries for use later, ıd here used four years later, showing com- :tations at 10% interest.

In Assignment of Error XIV, appellants claim ıat even if appellees were entitled to judg- nt against the Montana corporation, it was ror to give judgment against the Idaho sub- diary.

The Idaho corporation on its own petition, presented by its trustee, had itself made party defendant to the action. Had its signment been recorded, it would have been ought in originally by the appellees. It de itself a party, and the proof showed bad ith, and the taking of payments which were urious. Appellants admit in the wording

the very Assignment XIV: "The statute
so penalizes the person who is paid such
interest rate." Appellants brief, p. 14.
The District Judge made no error in giving
dgment against both corporation. The
nzarotti case squarely applied.

Respectfully submitted,

Stephen Bistline

Stephen Bistline
Attorney for Appellees
Sandpoint, Idaho

certify that, in connection with the pre-
ration of this brief, I have examined Rule
and 19 of the United States Court of Appeals
r the Ninth Circuit, and that, in my opinion,
e foregoing brief is in full compliance with
ose rules.

Stephen Bistline

Stephen Bistline